

S. S. Kresge Company Annual Report 1969

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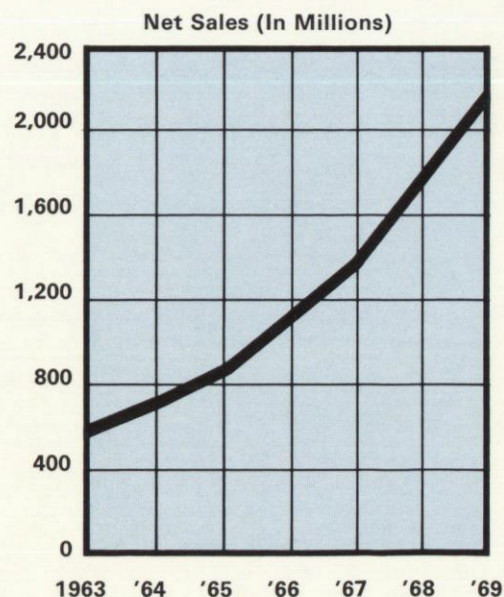
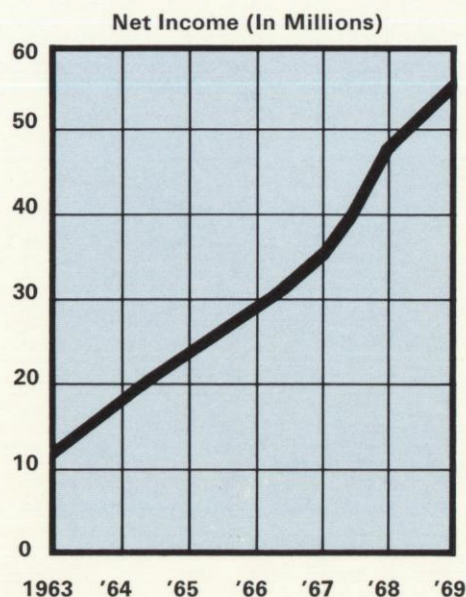
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1969 Highlights

	1969	1968
Sales	\$2,185,298,000	\$1,731,533,000
K mart, Kresge and Jupiter Stores	1,022	982
Net Income	\$ 54,089,000	\$ 47,611,000
Earnings Per Share of Common Stock:		
Assuming No Dilution	\$1.57	\$1.39
Assuming Full Dilution	\$1.52	\$1.35
Cash Dividends Declared Per Share	\$ 13,841,000 40¢	\$ 11,656,000 34¢
Employee Compensation and Benefits Per Sales Dollar	\$ 316,088,000 14.46%	\$ 254,688,000 14.71%
Depreciation and Amortization Per Sales Dollar	\$ 20,385,000 .93%	\$ 17,848,000 1.03%
Fixed Asset Additions	\$ 49,065,000	\$ 37,153,000



To the Shareholders:

Kresge's expansion program reached significant new dimensions in several areas during the fiscal year ended January 31, 1970.

In addition to opening a record number of new stores—65 K marts and one Kresge unit with a total sales area of approximately 4,700,000 square feet—two important new subsidiary companies were established, 85 major departments were taken over from K mart licensees and, after two years of experimental operations, a complete line of building supplies was incorporated into the standard merchandise assortment carried by most new U.S. K mart stores.

These activities added significantly to last year's consolidated sales increase of 26 percent and should contribute importantly to profits in 1970 and future years, but they had a negative effect on 1969 earnings.

Higher interest costs due to increased rates and heavier inventories also were an important factor in our slightly lower profit margin.

The creation of K mart Enterprises, Inc.—the subsidiary responsible for opening 56 K mart tire, battery and auto accessory departments in 1969—involved the formation of a complete new organization structure of executives, buyers, regional offices, district managers and departmental staffs before the first department was opened early last year. An intensive training program was expanded and accelerated as the new-store schedule reached a peak of 14 openings in the month of November. While this was an expensive undertaking, it was far less costly than the acquisition of our automotive licensee would have been. And we are pleased to report that this division is now functioning at a high level of efficiency, it is well prepared to open and operate some 70 new departments in 1970, and it should make an important contribution to consolidated profit this year.

Similar comments would apply to K mart (Australia) Limited, the company formed to open K mart stores in a joint venture with G. J. Coles & Coy. Ltd., of Australia. Five Australian K marts were opened in 1969—four after October 15, 1969, and a like number will open this year.

The U.S. K mart departments taken over from licensees and the new building supplies departments operated profitably, but they were partly responsible for higher-than-anticipated promotional markdowns



and shrinkage factors in our annual physical inventory calculations.

Despite the obvious uncertainties in today's economic environment, we are optimistic regarding your company's prospects for the current fiscal year. It may be somewhat more difficult to maintain the rate of sales increases that have typified Kresge's performance since 1963, but recent store-for-store comparisons have been surprisingly good, and it is anticipated that the K mart expansion program will exceed last year's 65-store schedule. We are in an excellent position to improve our profit margin if the overall business climate does not deteriorate more seriously than now seems likely.

For the longer term, there are exceptional opportunities for our business in the decade ahead. With continued growth in internally generated funds, plus the additional financing plans described in the following report, we shall proceed with a gradually enlarged expansion schedule while maintaining a traditionally conservative financial structure.

Our confidence regarding the future is most importantly based on the knowledge that the Kresge organization is broadly equipped to take advantage of the opportunities presented by the demographic and socio-economic forces that are so patently favorable to K mart's sector of general merchandise retailing.

A handwritten signature in dark ink, appearing to read "H. B. Cunningham". The signature is fluid and cursive, with a long, sweeping underline.

Chairman of the Board and President

Distribution

The price tag of every item in Kresge, K mart and Jupiter stores is substantially affected by the cost of its trip from the manufacturer to the store location. To make sure the merchandise is in stock when needed, competitively priced and still profit-producing, a specialized corps of Kresge's management team has developed an economical and reliable merchandise distribution system.

Distribution centers are an integral part of this system. Presently 25 percent of the merchandise sold in company stores is routed through these depots.

K mart expansion has necessitated a broadening and refining of the parent company's distribution center network in the last several years. In 1966 the parent company's only warehouse was a 730,000-square-foot structure in Fort Wayne, Indiana. A second distribution center was opened in Atlanta in 1967 and recently enlarged to just under 600,000 square feet. Sparks (Reno) was chosen as the site of the third center because of its proximity to California and the Northwest where the company is involved in a major K mart growth program. This newest unit of 450,000 square feet was opened in the summer of 1969 and is the largest roofed structure in Nevada.

Lawrence, Kansas, will be the location of a fourth distribution depot expected to begin operation in the spring of 1971. The Lawrence center will be the parent company's first semi-automated warehouse and its largest, approximately 1,000,000 square feet. Inbound merchandise will be loaded onto flatcars and, through the use of towveyor lines, will be routed automatically to any designated area. Empty flatcars will return to inbound docks by the same means. A large conveyor system will move filled orders into waiting trucks.

Goods moving through the parent company's distribution centers consists of imported items, repacked staples and, to a lesser extent, case-packed quantities of seasonable or promotional merchandise.

Approximately five percent of the company's volume is from imported items. This merchandise must be ordered early and often arrives three or four months in advance of its selling season. During the waiting period, millions of dollars' worth of goods is held temporarily at the various distribution centers. When the Lawrence struc-

ture begins operations, a portion of it will be used to house inactive imported merchandise until it is needed at the stores, while active imported articles will be allocated to Fort Wayne, Atlanta and Sparks.

Seventy percent of the merchandise moving through distribution centers consists of repacked items—goods ordered by the stores in less than case quantities. If a case contains 12 dozen, but a store needs only three dozen, the distribution center pulls an order for three dozen and repacks it along with other merchandise for the same store. In most cases, if a vendor were to ship only three dozen, the freight charges to the store would be prohibitive.

Generally, case-packed merchandise is handled by distribution centers only when this service to suppliers results in a price advantage for the Kresge Company. Some suppliers, lacking adequate warehousing and distribution facilities, prefer shipping in bulk to Kresge warehouses rather than routing small consignments directly to stores.

Merchandise is shipped from Fort Wayne, Atlanta and Sparks to stores principally through common carriers via truckloads, carloads or LTL (less than truckload). The company, through leasing arrangements, provides private trucking service from the Fort Wayne distribution center to Detroit and Chicago, where there are exceptionally heavy concentrations of stores.

The hub of the parent company's distribution network is the Fort Wayne center. Here a computer complex has been installed to serve the three existing depots and the Lawrence center to be constructed this year. The inventory of every item for each center is controlled by computer. Orders from the stores are optically scanned and create the input to the computer, which produces a combination store invoice and warehouse picking slip while simultaneously updating inventories. Information for the Atlanta and Sparks centers is transmitted to the respective centers via data transmission sets over a WATS (wide area telephone service) line.



Based on a two-year history of sales by item and giving effect to increase or decrease percentage factors, the computer generates purchase orders to the vendors to replenish inventories for all centers. It also produces various statistical reports for use by the buyers and sales department for analyzing item movement, dollar volume and warehouse profitability.

Holly Stores, Inc., the New York subsidiary responsible for the operation of women's and girls' ready-to-wear departments in U. S. K marts, moves approximately 90 percent of its goods through distribution center facilities. An effective computerized ticket re-order system keeps Holly management aware of style, color and size trends by store and area. With the majority of goods passing through distribution center facilities, Holly management can also exercise strict control of merchandise quality.

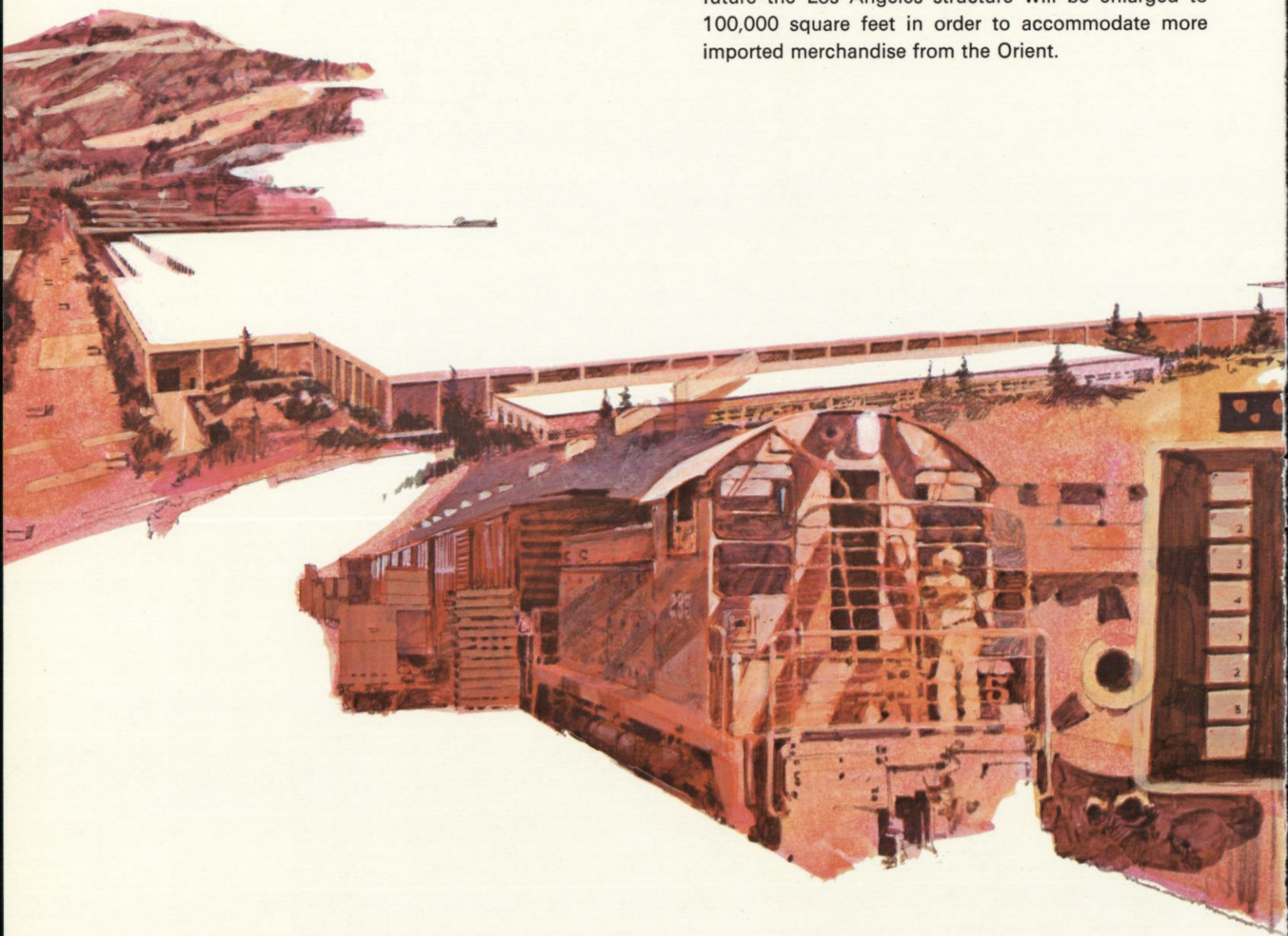
Holly's five warehouses, presently operating in the New York City area, will be consolidated in a 585,000-

square-foot distribution center now under construction in North Bergen, N. J., about 10 miles from the heart of New York's garment district. Upon completion in early 1971, it will be the most modern apparel warehouse in the Eastern part of the United States. The structure will also house Holly's administrative offices.

The North Bergen center will receive and distribute hangwear merchandise (dresses, coats and sportswear received as individual garments and hung on coat hangers) and flatwear (cartons of items requiring opening, processing and repacking for individual stores).

Automation will be emphasized in all operations that would normally require physical lifting or the transport of merchandise to specific operational areas. It is estimated that 65 to 80 percent of the entire operation will be automated.

In late 1969 Holly opened a 30,000-square-foot warehouse in Los Angeles to service about 100 stores in the parent company's Western Region with California-made ready-to-wear and some imported goods. In the near future the Los Angeles structure will be enlarged to 100,000 square feet in order to accommodate more imported merchandise from the Orient.



Holly also operates a 15,000-square-foot warehouse in Detroit as a merchandise processing center and storage facility for staple merchandise.

Plans for 1970 include the completion of a 40,000-square-foot warehouse in Atlanta and 20,000-square-foot depots in Pittsburgh and Chicago to service K mart's Southern, Eastern and Midwestern Regions. These three warehouses basically will handle staple merchandise and back-up stock for peak periods.

Kresge's other U. S. subsidiary, K mart Enterprises, Inc. of Royal Oak, Michigan, which operates K mart sporting goods and automotive departments, moves about 25 percent of its merchandise through distribution centers—a 107,000-square-foot warehouse adjacent to K mart Enterprises' headquarters and 25,000 square feet at the Sparks distribution center. The biggest volume of sporting goods, because of its bulkiness and weight, is drop-shipped by vendors directly to the stores. No automotive merchandise is presently moved through distribution centers.

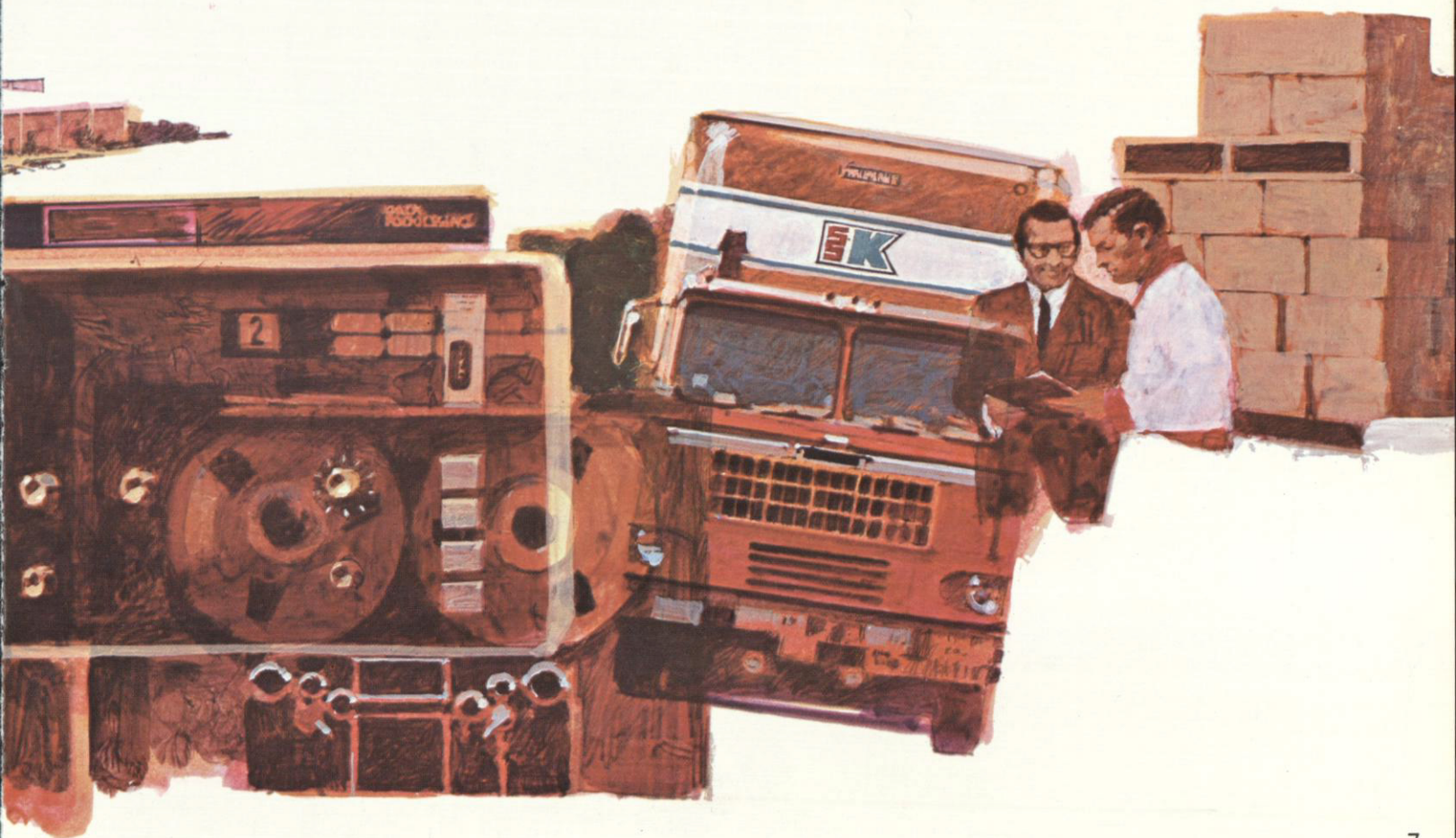
Important as distribution centers are, they obviously are only a partial answer to the Kresge Company's distribution needs. Small shipments (500 pounds or less) comprise the bulk of the 75 percent of Kresge's total merchandise that moves directly from suppliers to stores. By buying smaller amounts more frequently, stores have less investment in inventory, thus producing more rapid turnover and a higher return on investment. However, with constantly rising carrier rates, the distribution of these small shipments must be strictly controlled to avoid substantially increased "landed" costs.

Consolidator-distributors are one answer to Kresge's small-shipment problem. Consolidators accumulate small-package freight into large-volume shipments and forward it to stores. Moving small shipments in volume not only controls freight costs but assures merchandise being delivered on schedule.

Kresge's seven strategically located consolidator-distributors, owned and operated by consolidation agents, in most instances handle exclusively Kresge merchandise.

Several consolidation depots are now being built to Kresge specifications to be used solely by Kresge and operated by consolidation agents.

A Jersey City terminal is also on the drawing boards for completion in 1970. The 100,000-square-foot center





will house three major distribution operations. Packages will be consolidated primarily for stores on the East Coast, and imported merchandise will be pooled and forwarded. Incoming freight will be loaded in boxcars or in piggyback trailers (trucks moved by rail) for delivery to various consolidator-distributors and Kresge centers throughout the company's distribution network.

Shipper associations provide another answer to the small shipment problem. Such organizations of shippers combine tonnage to control freight costs. For example, the Chicago Shippers Association loads pool cars in New York City with merchandise for Kresge as well as other retailers for 42 destinations in the South, Southwest and Far West. The Kresge Company belongs to a dozen shipper associations and uses them to transport merchandise to geographical areas not covered by the consolidator-distributor program.

To further assure low freight costs and scheduled deliveries, Kresge headquarters provides each supplier with a routing guide indicating the type of transportation to be used for shipments to all stores.

The distribution system of Kresge's Canadian subsidiary, S. S. Kresge Company Ltd., is similar to the parent company's structure with a Toronto warehouse of 148,800 square feet filling the role performed by the parent company's Fort Wayne center. Additional distribution centers may be constructed in future years when warranted by expansion of the Canadian K mart program.

These are the primary elements of the Kresge Company's distribution system—employing a diversity of means to maintain an efficient and low-cost distribution system with the capability and flexibility necessary to keep pace with the company's aggressive K mart expansion program.

Financial and Operations Review

Consolidated sales of \$2,185,298,000 in 1969 were 26% above last year's record volume of \$1,731,533,000. Net income for the year was \$54,089,000, up 14% over net income of \$47,611,000 in 1968.

Earnings per share were \$1.57 compared with \$1.39 last year. On a fully diluted basis, earnings per share were \$1.52 in 1969 and \$1.35 in 1968.

Net Profit Margins

The rate of profit on sales was 2.48%, compared with 2.75% earned in 1968. Net earnings for 1969 represented a return on the stockholders' equity of 16.9%, down from the 1968 record of 17.3%, but ahead of the 1967 return of 14%.

The Kresge Company has experienced seven years of rapid profitable growth during the development of 338 K marts in the United States, Canada and Australia, and continued operation of Kresge and Jupiter variety stores in the United States and Canada. Our rate of increase in net income this year was less than the percent of increase in sales for several important reasons. Interest costs increased substantially, heavy U.S. and foreign start-up costs were incurred, and the company experienced a slight decline in gross profit margins due to heavier promotional markdowns and higher reported shrinkage.

Increased Interest Costs

Interest costs rose from \$5,656,000 in 1968 to \$9,766,000 in 1969, an increase of 73%. A principal contributing factor was the sharp rise in rate of interest. During 1968 the bank "prime rate" increased from 6% to 7%, and during 1969 the interest rate rose sharply to the historically high level of 8½%.

Interest costs also rose to cover the increase in short-term borrowings related to our credit sales, to finance the inventories in 65 new K marts, to cover the greater borrowing requirements associated with our new automotive departments, and the takeover of additional departments within our existing store units.

Start-up Costs

Effective February 1, 1969, K mart Enterprises, Inc., successor corporation to K mart Sporting Goods, Inc., operating through two divisions, became responsible for the operation of all sporting goods and new automotive departments in the parent company. A new

administrative, buying, and field force was established as a basis for a rapidly expanding tire, battery and auto accessory business in future years. Fifty-six automotive departments were opened during 1969, including all new United States K marts and three existing departments which had previously been operated by a licensee.

K mart (Australia) Limited, which was formed in 1968 to operate K mart stores in Australia, opened its first five stores in 1969. The first store opened on April 30 in Melbourne, and four stores opened late in the year—one in Perth, one in Sydney, and two in Adelaide. The openings were uniformly successful and the Kresge Company and G. J. Coles & Coy. Ltd., who respectively own 51% and 49% of the corporation, are optimistic about the potential for K mart's profitable growth in Australia. Four additional K marts are expected to open during 1970.

Expanded Merchandise Operations

During the past several years the Kresge Company has been expanding its capability in the merchandising of a number of departments previously operated by licensees. Eighty-five licensed departments were taken over by the company during 1969, including 30 men's wear, 17 home improvement and nine jewelry departments.

Late in the year a successful pharmacy company, operating in six K marts in the Southeast, discontinued its operations as a licensee and the management and professional staff were employed by the company.

There are no present plans to add pharmacies to all new K marts, but it is expected that an important expansion of Kresge-operated pharmacies will now be undertaken.

During 1969 the company increased the number of building materials departments. Twenty-one were in operation at yearend. After testing this department in selected stores, two new K mart prototypes were introduced to accommodate this 8,000- to 10,000-square-foot department and our "standard" 84,000-square-foot K mart (exclusive of the K mart food store) has been expanded to a 95,000- or 96,000-square-foot unit. The majority of new U.S. K marts built in 1970 will include this building materials department.

Gross Profit Margins

Late in 1969 retail sales demand began to soften at a time when we were entering the Christmas season with relatively heavy inventories. As a result of the mark-

downs taken to clean out seasonal merchandise and the greater promotional efforts to reduce stocks prior to the January 31 inventories, the company experienced reduced average gross margins and a decreased rate of profitability. Somewhat higher shrinkage associated with the heavy inventories was also incurred, particularly in certain departments taken over from licensees.

Federal Income Tax

The tax provision for 1969 was 50.5% of pretax income compared with 49.2% for 1968. The Federal income tax in both years includes the 10% Federal surcharge which represented a charge against earnings of \$4,607,000 or 13¢ per share in 1969 and \$3,519,000 or 10¢ per share in 1968.

The increase in the effective tax rate during 1969 was due to the reduction of the investment credit from \$1,624,000 to \$1,500,000 and to higher effective rates applicable to Holly Stores, Inc. and K mart Enterprises, Inc. At the time Holly Stores, Inc. and K mart Sporting Goods, Inc. (predecessor corporation to K mart Enterprises, Inc.) were acquired by Kresge, they were operating with multiple corporate structures. Under the Internal Revenue Service regulations, their composite tax rates reflected the fact that the first \$25,000 of annual income of each subsidiary corporation was exempt from corporate surtax.

As wholly owned subsidiaries become more profitable, producing earnings substantially in excess of \$25,000, the effect is to increase the corporate tax rate.

Under the provisions of the 1969 Tax Reform Act, the \$25,000 multiple surtax exemption will be gradually

reduced each year beginning in 1970 and will be phased out completely by January 31, 1975.

The tax provision was affected also by Australian operations, where losses were incurred for the year. The tax loss will be carried forward to apply against tax liabilities in future years.

The United States corporate income tax surcharge has been extended to June 30, 1970 at a 5% rate, or for five months of our 1970 fiscal year. In filing quarterly earnings statements, this surtax will be prorated against the full fiscal year's earnings and will represent 2.08% or 5/12 of 5%.

Management Training Program

All persons appointed to manage the 65 K marts opened in 1969 were career Kresge executives who had previously demonstrated their merchandising and leadership ability in successfully managing Kresge and Jupiter stores. Many of these managers had served as district managers of Kresge and Jupiter stores and the majority had also received K mart orientation while serving as K mart co-managers.

To meet the growing demand for management personnel, the company has expanded its management training efforts. Currently over 2,100 men are involved in this program designed to develop managers for their first Kresge or Jupiter store management assignments within four to six years after employment.

Of the trainees currently employed, over one-third are college graduates, one-third have two or more years of college and the other third are high school graduates.

SUMMARY OF SQUARE FEET OF SELLING AREA (000's)

	1962	1963	1964	1965	1966	1967	1968	1969
K mart Stores*								
United States	994	2,711	4,500	6,222	8,513	12,257	15,481	19,379
Canada	—	208	421	639	1,035	1,081	1,521	2,049
Australia	—	—	—	—	—	—	—	287
	994	2,919	4,921	6,861	9,548	13,338	17,002	21,715
Kresge Stores								
United States	8,382	8,548	8,376	8,199	7,735	7,366	7,143	6,910
Canada	1,064	1,056	1,109	1,089	1,066	1,045	1,032	959
	9,446	9,604	9,485	9,288	8,801	8,411	8,175	7,869
Jupiter Stores								
United States	271	326	494	682	802	857	835	795
Canada	23	23	18	19	24	24	24	90
	294	349	512	701	826	881	859	885
Grand Total	10,734	12,872	14,918	16,850	19,175	22,630	26,036	30,469

*Total store selling space exclusive of food supermarkets

During 1969 our college recruitment effort was particularly successful, and in the parent company 308 graduates were hired compared with 168 in 1968.

Our initial college recruiting efforts in 1970 appear even more promising than in 1969.

Capital Expenditures

Capital expenditures during 1969 amounted to \$49,065,000 compared with \$37,153,000 in 1968. Depreciation and amortization totaled \$20,385,000 compared with \$17,848,000 in 1968.

In addition to our normal new-store program covering the costs of furniture and fixtures and leasehold improvements, and our modernization and renovation program on existing stores, important investments totaling \$4,500,000 were made to build the Sparks distribution center and enlarge the Atlanta distribution center.

The investment tax credit allowed for fixed asset expenditures was suspended in April of 1969. Because our construction program was committed months ahead, the investment credit was \$1,500,000 this year compared with \$1,624,000 last year. The investment credit for 1969 would have been \$2,050,000 if it had not been suspended. It is expected that the investment credit for the current year will be reduced to approximately \$200,000.

Construction Program

Sixty-five new K marts were opened during 1969—53 in the United States, seven in Canada and five in Australia. One Kresge store previously destroyed by

fire was reopened. Nine Kresge stores were converted to Jupiter stores and 15 Kresge stores were permanently closed. The net increase in sales area amounted to about 4,433,000 square feet.

The Jupiter conversion program, while basically a defensive marketing plan, continues to provide an attractive alternative to the permanent closing of unprofitable Kresge stores. One hundred and eighteen Jupiter stores were in operation on January 31 and an additional four stores have been opened in 1970.

In the year that any Kresge or Jupiter store is closed prior to the expiration of a lease, the company follows the practice of charging to expense losses arising out of such early closings. Capital losses on the sale of store properties and the write-off on fixture disposals at the time of store closings are also expensed. Since the majority of store closings during 1969 involved lease expirations, our "loss on disposal" for 1969 was \$974,000, down from \$1,281,000 for 1968.

International Headquarters

In late 1969 ground was broken on a new international headquarters building in Troy, Michigan.

The 30-acre site is located on the northwest corner of Big Beaver and Coolidge Roads, approximately 20 miles from downtown Detroit.

The new building, comprising approximately 560,000 square feet, will be an assembly of self-contained units organized around a spine corridor system.

All units will be three stories high except a tower which will be four. Because of the changing and expanding

DIVISIONAL STORE SUMMARY

	K mart	Kresge	Jupiter	Total
Stores in operation February 1, 1969	273	593	116	982
Stores opened	65	—	—	65
Closed permanently	—	15*	7*	22*
Kresge stores converted to Jupiter in 1969	—	9*	9	—
Kresge stores closed temporarily for conversion (to be reopened as Jupiters)	—	4*	—	4*
Kresge store closed in 1967 for fire restoration—reopened in 1969	—	1	—	1
Net change	65	27*	2	40
Stores in operation January 31, 1970	338	566	118	1,022

*Reductions

requirements of the Kresge Company within its headquarters complex, a primary goal was to develop a flexible structure which would allow both realignment of operations within the building and construction of additional units as the need arises. It is expected that expansion will occur within the next 10 years.

The building exterior will be weathering steel and bronze glass and mahogany-colored architectural clay blocks. The weathering steel will require no maintenance and after a period of about five years will acquire a permanent, deep brown surface coating.

Target date for occupancy of the new facility is late 1971.

Preferred Stock

At the 1969 Annual Meeting stockholders approved a new class of capital stock consisting of 10,000,000 shares of no par value preferred stock. The stock may be issued in one or more series as determined by the Board of Directors and has voting and accumulative dividend rights. The stock was authorized primarily in the expectation that it might be advantageous in connection with possible mergers or acquisitions. None of the preferred stock has been issued and there

are currently no plans for its use.

Dividend Increase

Quarterly dividends were raised to 10¢ a share commencing with the June 12 payment compared with 8½¢ a share in effect during 1968—our fifth successive annual increase.

Long-Term Financing

The 4½% Convertible Debentures were called for redemption on April 20, 1970, but could be converted to common stock at the rate of \$24 a share before April 6, 1970. Because the conversion price is less than the current market price of the stock, it is expected that substantially all of the debentures will be converted. Earnings per share of \$1.52, assuming full dilution, gives effect to this assumed conversion.

In March of 1970 the company announced its intention to arrange the sale of \$125,000,000 in Convertible Subordinated Debentures. A registration statement (Form S-7) was filed with the Securities and Exchange Commission on March 19. The funds will be used to reduce short-term indebtedness and to facilitate our expansion program.

GEOGRAPHIC DISTRIBUTION OF STORES—JANUARY 31, 1970

	Number of Stores by Type			
	K mart	Kresge	Jupiter	Total
UNITED STATES				
Eastern Region Connecticut, Delaware, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Vermont	19	112	25	156
Central Region Indiana*, Michigan*, Ohio*, West Virginia*	60	165	22	247
Midwestern Region Illinois*, Indiana*, Iowa, Kansas, Michigan*, Minnesota, Missouri, Nebraska, North Dakota, South Dakota*, Wisconsin	53	104	48	205
Southern Region Alabama, Arkansas, Florida, Georgia, Illinois*, Indiana*, Kentucky, Louisiana, Maryland, North Carolina, Ohio*, South Carolina, Tennessee, Texas*, Virginia, West Virginia*, District of Columbia, Puerto Rico	104	89	10	203
Western Region Arizona, California, Colorado, Idaho, Montana, Nevada, New Mexico, South Dakota*, Texas*, Utah, Washington, Wyoming	64	17	—	81
CANADA				
Alberta, British Columbia, Manitoba, Ontario, Quebec, New Brunswick, Nova Scotia, Saskatchewan	33	79	13	125
AUSTRALIA				
New South Wales, South Australia, Victoria, West Australia	5	—	—	5
GRAND TOTAL	338	566	118	1,022

*Includes only part of state

Consolidated Statement of Income

	Fiscal year ended January 31	
	1970	1969
Sales	\$2,185,298,000	\$1,731,533,000
Fees from licensed departments	31,566,000	26,217,000
Interest income	1,279,000	1,318,000
	<u>2,218,143,000</u>	<u>1,759,068,000</u>
Cost of merchandise sold (including buying and occupancy costs)	1,658,953,000	1,303,595,000
Selling, general and administrative expenses	439,111,000	354,825,000
Interest expense	9,766,000	5,656,000
Loss on disposals of fixed assets and cancellation of leases	974,000	1,281,000
	<u>2,108,804,000</u>	<u>1,665,357,000</u>
Income before estimated income taxes	109,339,000	93,711,000
Estimated income taxes (Note B) :		
U.S., less investment credit of \$1,500,000 and \$1,624,000, respectively	46,598,000	37,143,000
Foreign	5,760,000	5,934,000
Tax effects of timing differences	2,892,000	3,023,000
	<u>55,250,000</u>	<u>46,100,000</u>
Net income for the year	<u>\$ 54,089,000</u>	<u>\$ 47,611,000</u>
Earnings per share of common stock (Note E) :		
Assuming no dilution	\$1.57	\$1.39
Assuming full dilution	<u>\$1.52</u>	<u>\$1.35</u>

Consolidated Balance Sheet

ASSETS	January 31	
	1970	1969
Current Assets:		
Cash	\$ 46,796,000	\$ 25,814,000
Certificates of deposit	1,850,000	2,775,000
Marketable securities, at cost approximating market	5,897,000	21,097,000
Customer accounts receivable, less allowance for possible losses of \$9,462,000 and \$5,405,000, respectively	93,512,000	80,447,000
Other accounts receivable	6,870,000	9,616,000
Merchandise inventories at lower of cost (approximate first-in, first-out) or market	399,586,000	304,236,000
Operating supplies and prepaid expenses	13,150,000	9,815,000
Total current assets	567,661,000	453,800,000
Other Assets and Deferred Charges	3,922,000	3,390,000
Fixed Assets, at cost:		
Land	35,707,000	35,263,000
Buildings	65,532,000	57,170,000
Leasehold improvements	73,755,000	71,125,000
Furniture and fixtures	213,625,000	185,290,000
Construction in progress	5,872,000	6,324,000
	394,491,000	355,172,000
Less—Depreciation and amortization	168,548,000	154,537,000
	225,943,000	200,635,000
	<u>\$797,526,000</u>	<u>\$657,825,000</u>

LIABILITIES	January 31	
	1970	1969
Current Liabilities:		
Portion of long-term debt due within one year (Note C)	\$ 1,762,000	\$ 1,756,000
Notes payable to banks	103,896,000	58,850,000
Accounts payable—trade	158,743,000	115,807,000
Accrued payrolls, taxes and other liabilities	54,221,000	46,646,000
Dividends payable	3,469,000	2,925,000
U.S. and foreign income taxes (Note B)	27,635,000	29,295,000
Total current liabilities	<u>349,726,000</u>	<u>255,279,000</u>
Long-Term Debt , less portion due within one year (Note C)	57,753,000	61,190,000
Deferred U.S. and Foreign Income Taxes (Note B)	22,528,000	21,384,000
Minority Interest in Australian Subsidiary		522,000
Stockholders' Equity (Note D) :		
Common stock (Note G)	57,855,000	57,406,000
Capital in excess of par value	20,871,000	13,499,000
Income retained for use in the business (Note C)	289,131,000	248,883,000
	<u>367,857,000</u>	<u>319,788,000</u>
Less—27,718 shares in treasury at cost	338,000	338,000
	<u>367,519,000</u>	<u>319,450,000</u>
	<u>\$797,526,000</u>	<u>\$657,825,000</u>

Consolidated Statement of Income Retained

	Fiscal year ended January 31	
	1970	1969
Income retained for use in the business at beginning of year	\$248,883,000	\$212,928,000
Net income for the year	54,089,000	47,611,000
Cash dividends declared—40¢ and 34¢ a share, respectively	(13,841,000)	(11,656,000)
Income retained for use in the business at end of year	<u>\$289,131,000</u>	<u>\$248,883,000</u>

Consolidated Statement of Source and Application of Funds

	Fiscal year ended January 31	
	1970	1969
Source of Funds:		
Net income	\$54,089,000	\$47,611,000
Depreciation and amortization (principally straight-line)	20,385,000	17,848,000
Increase in deferred U.S. and foreign income taxes	1,144,000	1,123,000
Sales of fixed assets	3,372,000	3,609,000
Sales of common stock under stock option and purchase plans	6,219,000	4,457,000
Increase in notes and mortgages payable		2,951,000
Minority interest in Australian subsidiary		522,000
	<u>\$85,209,000</u>	<u>\$78,121,000</u>
Application of Funds:		
Additions to fixed assets	\$49,065,000	\$37,153,000
Cash dividends declared	13,841,000	11,656,000
Reduction of notes and mortgages payable	1,762,000	1,756,000
Other	1,127,000	395,000
Increase in working capital	19,414,000	27,161,000
	<u>\$85,209,000</u>	<u>\$78,121,000</u>

Opinion of Independent Accountants

TO THE STOCKHOLDERS AND BOARD OF
DIRECTORS OF S. S. KRESGE COMPANY

In our opinion, the accompanying consolidated balance sheet, the related consolidated statements of income and income retained for use in the business and the statement of source and application of funds present fairly the financial position of S. S. Kresge Company and its subsidiary companies at January 31, 1970, the results of their operations and the supplementary information on funds for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Our examination of these statements was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

211 West Fort Street
Detroit 48226
March 16, 1970

PRICE WATERHOUSE & CO.

Notes to Consolidated Financial Statements

(A) Basis of Consolidation:

All subsidiary companies have been included in the consolidated financial statements. In consolidation the assets, liabilities and operations of the foreign subsidiaries were translated into U.S. dollars at appropriate rates of exchange. For the year ended January 31, 1970 the assets and net income of the foreign subsidiaries amounted to approximately 12% and 8% of the consolidated assets and net income, respectively.

(B) Income Taxes:

The current liability for U.S. and foreign income taxes includes \$6,688,000 at January 31, 1970 and \$5,100,000 at January 31, 1969 arising from the tax effects of timing differences related principally to profit on installment sales. The amounts shown on the balance sheet for Deferred U. S. and Foreign Income Taxes result from the difference between book and tax depreciation.

(C) Long-Term Debt:

4½% convertible subordinated debentures	\$35,031,000
3½% and 4½% notes, payable in varying amounts through December 16, 1983 (\$1,625,000 due within one year)	20,000,000
Other	4,484,000
	<u>59,515,000</u>
Portion due within one year	1,762,000
	<u>\$57,753,000</u>

The debentures due June 15, 1992 are convertible into common stock at \$24 a share. The debentures have been called for redemption on April 20, 1970 at 103.625% of the principal amount together with accrued interest to the redemption date. At January 31, 1970, 1,459,617 shares of unissued common stock are reserved for conversion. The expenses relating to the sale of the debentures are being amortized to income over the term of such debentures on the bonds outstanding method and, upon conversion of debentures, the applicable amount of unamortized expense is charged to capital in excess of par value. At January 31, 1970, the balance of unamortized expense approximated \$700,000.

The agreements relating to the notes payable and the indenture relating to the debentures restrict the payment of dividends (other than stock dividends) and the purchase or retirement of shares of the Company's capital stock. Under the most restrictive of these covenants, income retained of approximately \$150,000,000 is free from such restrictions at January 31, 1970.

Principal payments on long-term debt for the five years ending January 31, 1975 are as follows:

1971	\$1,762,000
1972	1,767,000
1973	1,774,000
1974	4,592,000
1975	1,785,000

(D) Stockholders' Equity:

In May, 1969 the stockholders approved an amendment to the Articles of Incorporation of the Company which, among other things, created a new class of capital stock consisting of 10,000,000 shares of preferred stock, no par value. Such shares have voting and cumulative dividend rights and may be issued in one or more series as determined by the Board of Directors. All shares will be identical except that there may be variations in different series with respect to dividend rate, redemption price, liquidation preference, sinking fund provisions and conversion features. No preferred stock had been issued as of January 31, 1970.

Changes in stockholders' equity, other than income retained for use in the business, were as follows:

	Common Stock— (authorized 60,000,000 shares of \$1.66 ½ par value)		Capital in excess of par value
	Shares	Amount	
Balance January 31, 1969	34,443,591	\$57,406,000	\$13,499,000
Common stock sold to officers and employees under stock option and purchase plans	199,788	333,000	5,886,000
Conversion of debentures	69,680	116,000	1,486,000
Balance January 31, 1970	<u>34,713,059</u>	<u>\$57,855,000</u>	<u>\$20,871,000</u>

(E) Earnings Per Share of Common Stock:

"Earnings per share of common stock—assuming no dilution" were computed by dividing net income by the weighted average number of shares of common stock outstanding during each year.

"Earnings per share of common stock—assuming full dilution" were determined on the assumption that the 4½% convertible debentures were converted at the beginning of each year. Net earnings were adjusted for interest expense and amortization of debenture expense net of the related tax effect. In making the computation for the year ended January 31, 1970, the number of common shares was also increased by the number of shares issuable on the exercise of stock options from the date such options were granted and by the number of shares issuable under the employee stock purchase incentive plan. This increase in the number of common shares was reduced by the number of common shares which are assumed to have been purchased with the proceeds from the exercise of the stock options and with the contributions to the stock purchase incentive plan; these purchases were assumed to have been made at the market price at January 31, 1970.

"Earnings per share of common stock—assuming no dilution" would have been \$1.52 for the year ended January 31, 1970 had all of the 4½% convertible debentures been converted on February 1, 1969. This computation is based on the assumption that all of the debentures called for redemption will be converted rather than redeemed.

(F) Retirement Income Plans:

The Company and its subsidiaries have non-contributory retirement pension plans covering most employees, whose eligibility is based on age and years of service. The total pension expense was \$4,335,000 and \$3,363,000 for the years ended January 31, 1970 and 1969, respectively. The Company's policy is to fund pension costs accrued.

(G) Stock Option and Purchase Incentive Plans:

Under a qualified stock option plan approved by the stockholders in May 1969, options to purchase 400,000 shares of common stock may be granted to officers and key employees at 100% of the fair market value on the date of grant. Options expire five years from the date of grant and are exercisable in annual installments, except that options granted to optionees over age 61 at the date of grant are exercisable in total at such date.

Information on stock purchase incentive and option plans is summarized below:

	Number of shares
Stock purchase incentive plan—	
Shares available for purchase at January 31, 1969 at 85% of market value	1,036,546
Shares purchased during the year through payroll deduction at \$30.98 a share	197,103
Shares available for purchase at January 31, 1970	<u>839,443</u>
Stock option plan—	
Under option at January 31, 1970 (\$41.88 to \$56.69 per share)	210,555
Options which became exercisable during the year (\$41.88 to \$56.69 per share)	43,340
Options exercised during the year at \$41.88 per share	2,685
Available for grant at January 31, 1970	<u>186,760</u>

(H) Commitments:

Minimum annual rentals under 1,087 leases for stores occupied at January 31, 1970 aggregated \$76,473,000. These leases expire during ten year periods ending January 31, as follows:

1980	\$10,842,000
1990	38,323,000
2000	26,331,000
2001 to 2035	977,000
	<u>\$76,473,000</u>

Certain leases provide for additional rents based on sales volume in excess of a specified base, and certain other leases provide for taxes and other expenses.

Purchase commitments and construction obligations in connection with the Company's expansion program amounted to approximately \$8,000,000 at January 31, 1970.

(I) Subsequent Event:

On March 19, 1970 the Company intends to file a registration statement with the Securities and Exchange Commission seeking registration of \$125,000,000 Convertible Subordinated Debentures due in 1995. See Financial and Operations Review for further comments.

10-Year Financial Review

<i>(Dollar amounts shown in thousands)</i>	1969	1968	1967
Sales	\$2,185,298	\$1,731,533	\$1,385,694
Net Income	\$ 54,089	\$ 47,611	\$ 34,915
% to Sales	2.48%	2.75%	2.52%
Earnings Per Share of Common Stock:			
Assuming No Dilution	\$ 1.57	\$ 1.39	\$ 1.03
Assuming Full Dilution	1.52	1.35	1.02
Cash Dividends Declared	\$ 13,841	\$ 11,656	\$ 10,188
Per Share	.40	.34	.30
K mart, Kresge and Jupiter Stores	1,022	982	943
Inventories of Merchandise	\$ 399,586	\$ 304,236	\$ 223,933
% to Sales	18.29%	17.57%	16.16%
Net Working Capital	\$ 217,935	\$ 198,521	\$ 171,360
% to Sales	9.97%	11.47%	12.37%
Net Worth	\$ 367,519	\$ 319,450	\$ 275,632
Per Share	10.66	9.34	8.13
Long-Term Debt	\$ 57,753	\$ 61,190	\$ 63,476
Fixed Asset Additions less Retirements	\$ 45,693	\$ 33,544	\$ 26,866

Per share calculations give effect to 1968 three for one and 1966 two for one stock splits

1966	1965	1964	1963	1962	1961	1960
\$1,090,181	\$851,443	\$688,776	\$543,671	\$483,013	\$450,605	\$434,945
\$ 28,609 2.62%	\$ 22,154 2.60%	\$ 17,374 2.52%	\$ 11,089 2.04%	\$ 9,053 1.87%	\$ 9,197 2.04%	\$ 11,403 2.62%
\$.85	\$.67	\$.53	\$.34	\$.27	\$.28	\$.35
\$ 8,702 .26	\$ 7,761 .23	\$ 6,602 .20	\$ 6,607 .20	\$ 8,273 .25	\$ 8,829 .27	\$ 8,829 .27
915	895	885	854	821	777	759
\$ 166,084 15.23%	\$136,187 15.99%	\$108,266 15.72%	\$ 90,796 16.70%	\$ 81,172 16.81%	\$ 72,501 16.09%	\$ 67,786 15.58%
\$ 123,798 11.36%	\$110,739 13.01%	\$ 93,362 13.55%	\$ 83,969 15.44%	\$ 63,595 13.17%	\$ 62,891 13.96%	\$ 62,371 14.34%
\$ 251,803 7.48	\$229,597 6.91	\$212,419 6.44	\$202,544 6.14	\$197,996 5.99	\$198,270 5.99	\$196,843 5.95
\$ 26,254	\$ 27,869	\$ 29,407	\$ 31,182	\$ 16,983	\$ 18,332	\$ 19,752
\$ 22,720	\$ 13,188	\$ 14,724	\$ 12,638	\$ 11,739	\$ 10,083	\$ 11,783

S. S. Kresge Company, A Michigan Corporation

Executive Offices
2727 Second Avenue
Detroit, Michigan 48232

Subsidiaries

S. S. Kresge Company Limited
Toronto, Ontario, Canada

Holly Stores, Inc.
New York, New York

K mart (Australia) Limited
Melbourne, Victoria, Australia

K mart Enterprises, Inc.
Royal Oak, Michigan

Officers

Harry B. Cunningham, *Chairman of the Board and President*
Claude M. Booker, *Executive Vice President, Merchandising*
Robert E. Dewar, *Executive Vice President, Administration and Finance*
Fred K. Nieman, *Executive Vice President, Store Management and Operations*
John B. Hollister, *Senior Vice President, Real Estate*
Robert H. Griffin, *Vice President, K mart Operations*
William R. Marshall, *Vice President, Merchandising Subsidiaries and K mart Licensees*
Henry G. McIntosh, *Vice President, Management Services*
Ralph E. Phelps, *Vice President, General Counsel and Secretary*
Harold A. Siegel, *Vice President, Food Operations*
Walter H. Teninga, *Vice President, Corporate Growth*
Raymond E. Valley, *Vice President, Management Personnel*
Ervin E. Wardlow, *Vice President, Sales*
Lee W. Zane, *Vice President, Employee Relations and Store Personnel*
Clyde K. Bowles, *Vice President, Southern Region*
Bernard M. Fauber, *Vice President, Western Region*
David D. Matson, *Vice President, Eastern Region*
Grant W. Morck, *Vice President, Central Region*
Robert J. Young, *Vice President, Midwestern Region*
Richard H. Black, *Treasurer*
Dale A. Feet, *General Controller*

Directors

Arnold H. Bachner
William H. Baldwin
Claude M. Booker
Morgan Collins
Harry B. Cunningham
Robert E. Dewar
John B. Hollister
Stanley S. Kresge
Rolland Lawson
Fred K. Nieman
Donald F. Valley

Executive Committee

Harry B. Cunningham, *Chairman*
Claude M. Booker
Robert E. Dewar
Fred K. Nieman
Donald F. Valley

Finance Committee

Donald F. Valley, *Chairman*
William H. Baldwin
Richard H. Black
Morgan Collins
Harry B. Cunningham
Robert E. Dewar

Transfer Agents

National Bank of Detroit
Detroit, Michigan

The Chase Manhattan Bank N. A.
New York, New York

Registrars

Manufacturers National Bank
of Detroit
Detroit, Michigan

First National City Bank
New York, New York

Trustee—4½% Convertible
Subordinated Debentures
National Bank of Detroit
Detroit, Michigan

Annual Meeting

The Annual Meeting will be held the third Wednesday of June (June 17, 1970) at 10 a.m. at the Masonic Temple, 500 Temple Avenue, Detroit, Michigan.

